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Clerk
Michigan Supreme Court
925 W. Ottawa
Lansing, MI 48933

March 6, 2003

Re: ADM File 2002-38

In lieu of the dues increase being sought by the State Bar of Michigan to underwrite the Client Security Fund, and as a matter of good public policy, I propose a new court rule and State Bar Rule to protect the public from dishonest lawyers.

The Client Security Fund is a gratuitous program, whereby honest lawyers are made to repay the peculations of dishonest ones. Not only is the program wrong in concept—there should not be a financial penalty for honesty—but it is wrong in execution as well. As currently structured, the CSF has no legal status and no legal liability. Run by the State Bar as a little fiefdom answerable to no one, the CSF gives (in the true sense of donation) compensation to some victims of lawyer thievery and not to others; it does so at whim, and there is no element of judicial review or due process that is required. Identical applicants may be treated disparately, and they have no remedy, because the CSF has no legal obligation to pay anybody anything, to treat anyone fairly, or to follow any constitutional or statutory requirements of any kind. Thus, the message of the CSF to the public is, "We lawyers are worried about dishonest members of our profession enough to make gifts of money to a few people as a public relations gesture, but not enough that we are willing to recognize any legal obligation on our part to do anything."

The burden of lawyer dishonesty currently falls on victims directly, and on State Bar members generally. Some victims fall outside the purview of the CSF, on a theory they should have protected themselves; no intellectually rigorous or empirically justifiable data support this invidious discrimination and gratuitous paternalism. Other victims are regarded as sufficiently subject to being duped as to be protected from their own bad decisions in choosing dishonest lawyers, as though the market forces and law enforcement authorities that suffice in every other field of human endeavor magically disappear when lawyers come on the scene.

The problem should be viewed as one in a commercial field. Just as all motor vehicle owners have to procure no-fault insurance (and, under former practice, had to contribute to the state accident fund if they did not have liability insurance), to support a minimum financial protection for all potential motor vehicle accident victims, lawyers who handle client funds should be regarded as a subset of the legal profession which profits from doing so, and which should be regulated to maintain the free flow of the market.

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The proper form of regulation is mandatory bonding, combined with the use of mandatory escrow arrangements. Thus, the first step is a new State Bar Rule (or an amendment to the IOLTA Rule) requiring that lawyers who handle client funds be bonded. While commercial enterprises already exist to provide such bonding coverage, the State Bar can also, as it did with legal malpractice insurance, form its own underwriting company, to assure bonding at reasonable cost and to discourage price gouging in a possibly oligopolistic insurance market. The rule would provide something like this:

SBR 18 Bonding for Lawyers Who Handle Client Funds

(a) All lawyers and law firms, as a precondition to controlling, managing, possessing, or having authority over client or trust funds of any kind and in any amount must be bonded as required by this Rule.

(b) A fidelity bond must be in a minimum amount equal to 125% of the total client and trust funds controlled, managed, possessed or held under the lawyer's or law firm's authority, but in no event less than $100,000.

(c) A fidelity bond must be issued by an insurer licensed to do business in the State of Michigan.

(d) A fidelity bond certificate, specifying the current amount of the fidelity bond then in force for a lawyer or law firm, shall be prominently displayed at the lawyer's or law firm's offices. Such a certificate shall be deemed the property of the insurer which issued it, and must be immediately returned to the insurer if any bonding premium is not timely paid, or if the bond is canceled, withdrawn, or otherwise terminated.

(e) A copy of the lawyer's or law firm's current fidelity bond certificate as specified in subparagraph (d) hereof shall be filed with the lawyer's annual payment of dues to the State Bar of Michigan; in any event, even where no dues is payable or where dues is not timely paid, the certificate must be filed not later than the deadline for making timely payment of dues without penalty. Each member shall, as part of the annual dues reporting requirement, certify to the State Bar in writing the total client and trust funds controlled, managed, possessed or held under the lawyer's authority in the prior membership year and within three months of the dues payment deadline.

(f) The Attorney Grievance Administrator shall be designated a party in interest on all fidelity bonds issued in fulfillment of this Rule, and insurers shall notify the Attorney Grievance Administrator promptly when any fidelity bond is canceled, withdrawn, or terminated for any reason.

(g) Violation of any part of this Rule shall be deemed misconduct prejudicial to the administration of justice and subject the violator (and for law firms every member and associate thereof) to disciplinary action.

(h) Any lawyer who violates this Rule and causes thereby an uninsured loss to a client or trust shall be, at a minimum, suspended from the practice of law until the client or trust is fully repaid, with interest, attorney fees, and costs, and until the State Bar or Grievance Administrator is fully repaid for all costs of investigation, discipline, and enforcement.

Additionally, there needs to be a court rule providing for escrow of client funds, thereby eliminating at the source one of the major means by which client funds have been subjected to lawyer depredations.

MCR 2.619 Mandatory Escrow of Settlement and Judgment Payments

(A) When any action results in a judgment or settlement whereby one party becomes obligated to pay money to another party, such payment shall be made only to the Clerk of the court in which judgment was entered or in which a pending action was settled.

(B) Any settlement or consent judgment must contain in boldface type at least two points larger than the largest type otherwise used for the document reflecting the terms of the settlement or judgment the following provision immediately before the first signature line:

Notice: Pursuant to MCR 2.619, any payment made to satisfy this [settlement] [judgment] must be made to the Clerk of the [court in which case pending]. The Clerk will then disburse the funds received to the party, parties, or attorney(s) entitled to them, pursuant to the Court's direction.

(C) Clerks of the circuit, district, probate and municipal courts shall receive such funds and place them in one or more interest bearing escrow accounts, and report to the assigned judge weekly as to funds received. The Clerk shall also report to the parties entitled to receive such payments and to their attorneys of record, within one week of receipt, that such funds have been deposited. One-half the interest earned on such funds shall be retained by the Clerk to defray the expenses of administration of this rule; the remainder shall be paid pro rata to the persons entitled to the judgment or settlement proceeds.

(D) The court, upon being informed that funds are available for disbursement, shall enter an appropriate order directing the Clerk to whom funds shall be paid and in what amount. The court may, on the basis of information previously furnished by the parties and attorneys as to their arrangements, enter a disbursement order without a hearing, or shall schedule a prompt hearing to determine the proper disbursement of the funds received. If, by the time set for hearing, the parties entitled to receive payment and their attorneys have not stipulated to disbursement, the court shall hear the matter and direct disbursement as appropriate.

(1) Where the parties and their attorneys have stipulated to disbursement, the Clerk shall make such disbursement forthwith in accordance with the stipulation.

(2) Where the court directs disbursement, MCR 2.614(A)(1) applies.

(3) An attorney entitled to a lien on any judgment or settlement proceeds may file a notice of lien with the Clerk, and, for purposes of this rule only, shall be deemed an attorney of record entitled to notice and opportunity to be heard as to any disbursement.

(4) Disputes between clients and attorneys over fees and costs may be resolved under this rule without any need for filing a separate action or motion. Any order so made shall be deemed a final order pursuant to MCR 7.202(7)(iv).

(E) Any sheriff who has funds after execution or attachment or from any sheriff's sale conducted to satisfy a judgment may pay such funds to the Clerk of the court issuing the judgment, whereupon such funds shall be treated as having been paid by the judgment debtor and deposited and disbursed under this rule. The sheriff shall thereupon be absolved of further responsibility for the funds so paid.

(F) Any garnishee defendant may, in lieu of making payment to the garnishor, pay garnished funds to the Clerk of the Court issuing the garnishment order.

(1) The State Court Administrator shall modify the approved garnishment forms to reflect the provisions of this rule.

(2) Upon making payment to the Clerk, the garnishee defendant shall be thereupon absolved of further liability to the extent of the funds so paid.

(3) Funds so paid to the Clerk shall be treated as having been paid by the judgment debtor and deposited and disbursed under this rule.

These rules eliminate the need to raise State Bar dues to fund the no longer useful Client Security Fund, which may be abolished. Under these new rules, victims of attorney embezzlement have a legal right to file a claim with the bonding company, which is subject to due process and judicial review, making this system far superior to the CSF.

Very truly yours,

Allan Falk (P13278)